IN THE

Supreme Court of the United States

OCTOBER TERM, 1964

No. 1209

STANLEY JACHIMIEC, individually and on behalf of all other similarly situated shareholders of SCHENLEY INDUSTRIES, INC., *Petitioner,*

v.

SCHENLEY INDUSTRIES, INC., a corporation, et al., *Respondents.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF RESPONDENT SCHENLEY INDUSTRIES, INC. IN OPPOSITION

THE QUESTION PRESENTED

Does a shareholder of a corporation who did not tender his stock and who is neither a purchaser nor a seller, have standing to enjoin the corporation from consummating the purchase of its shares from tendering shareholders on his claim that the corporation's Invitation for Tenders violated Rule 10(b)-5?

STATEMENT

This, in its present posture, is a suit by a person who has not been injured or threatened with injury, on behalf of a class of which he is not a member, to enjoin a transaction already consummated, on the ground that Schenley has paid too high a price for its shares to stockholders who thereby received too low a price for the very same shares in the very same transaction.

On January 28, 1965, Schenley mailed to its shareholders an Invitation for Tenders (herein "the Invitation") offering to purchase 1,000,000 shares of its outstanding common stock at $32 per share and stating that such a purchase had been determined by the Board of Directors to be in the best interests of the corporation. Shares were to be tendered on or before February 11, 1965, and provision was made for pro rata acceptance if more than 1,000,000 shares were tendered. The Invitation accurately set forth the range of market prices (from a high of 37⅜ in 1960 to a low of 15⅝ in 1962) for 5 years plus 26 days, and also the last sale price (27¼) immediately before the Invitation. It referred to the financial statements for the fiscal year ended August 31, 1964, contained in its Annual Report previously mailed to shareholders and offered to supply additional copies on request. It went on to provide summary sales and earnings data for the subsequent 4 months ended December 31, 1964, the latest month-end prior to the date of the Invitation, and to show precisely how these earnings compared with those for the same 4 months of the prior year.

The Invitation also stated that the offer to purchase was not open to any officer or director or his "associates" as that term is defined in rules of the Securities and Exchange Commission. It further stated that approaches had been made to certain major stockholders indicating an interest in the purchase of their shares, but that such approaches had not been definitive as to price or otherwise and the

corporation had no knowledge as to whether they would be renewed or whether offers might be forthcoming to other shareholders.

Count I of the complaint was based essentially on Section 10(b) of the Securities Exchange Act of 1934 and Rule 10(b)-5 thereunder. Count II incorporated all of the substantive allegations of Count I and, on the basis thereof, alleged mismanagement, breach of fiduciary duty and other matters of concern under the Delaware corporation law.

The District Court granted a preliminary injunction without hearing any evidence. An interlocutory appeal was taken immediately.

The Court of Appeals, on the interlocutory appeal, dissolved the injunction and remanded the case with instructions to dismiss Count I of the two count complaint. The action of the Court of Appeals did not affect Count II, which is still pending.

The Court of Appeals ordered Count I dismissed in conformity with a decision of the Court of Appeals for the Second Circuit, *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2nd Cir. 1952), cert. denied 343 U.S. 956 (1952), and because the matters and things alleged in the Complaint or disclosed by the record are not violative of or tend to show any violation of Rule 10(b)-5.[1]

The judgment of the Court of Appeals can be reversed only if neither ground can be supported.

Plaintiff's several improper attempts to supplement the record in his Petition do not call for response here except to point out one significant misstatement of fact.

---

[1] As the Court of Appeals found, the Invitation for Tenders was not deceptive, fraudulent or insufficient. The common stock of Schenley is listed on the New York Stock Exchange. The company is consequently subject to the continuous disclosure system of Sections 13 and 14 of the Securities Exchange Act of 1934 and, as

The plaintiff on page 9 of his Petition for Certiorari goes outside the record to refer to a newspaper report of March 25, 1965 of Schenley's net income and earnings for the six months ended February 28, 1965, published almost a month after the decision of the Court of Appeals. Plaintiff's contention that this report reflects "extraordinarily improved earnings" is based on the device of not using the same factors for the periods being compared.[2]

The Invitation itself showed an increase in earnings from $.54 to $.92 per share in the comparable figures for the four months ended December 31, 1963 and December 31, 1964 respectively (an increase of 70%). Comparable figures for the six months ended February 28, 1964 and February 28, 1965 respectively, based upon the number of shares outstanding after the purchase of 1,000,000 shares pursuant to the Invitation to Tender, would show an increase from $1.10 to $1.88 per share (an increase of 71%).

In any event the concept of "full" or even "timely" disclosure does not require a company to forecast its earnings for a period ending one month after the making of its offer to purchase.

---

stated in the Invitation for Tenders, the Company's financial statements for its fiscal year ended August 31, 1964, were contained in its Annual Report for that period mailed to shareholders prior to the Annual Shareholders' meeting on December 10, 1964. There was also sent to the shareholders prior to the Annual Meeting a Proxy Statement which had full information as to the shares of the Company owned by Lewis S. Rosenstiel and his "associates." Plaintiff has received Annual Reports and Proxy Statements each year since 1954 when he alleges he became a shareholder. Rule 10(b)-5 does not require that all or any part of this publicly available information be restated in an offer to purchase shares. There is no issue as to the accuracy of any of this information.

[2] $.71 per share attributable to the sale of an investment is a non-recurring capital gain which obviously must be disregarded in measuring the operational earnings trend. Likewise, Schenley's interest in the earnings of Buckingham Corporation, which was acquired on August 31, 1964, cannot be considered since such earnings were not included in the figures for the six months period ending February 28, 1964.

REASONS FOR DENYING THE WRIT

1. The ruling of the Court of Appeals applies a doctrine long established by sound judicial, administrative and legislative action. There is no conflict in the authorities.

The plaintiff, who did not accept Schenley's Invitation for Tenders, was not and is not a seller of securities. In *Birnbaum* v. *Newport Steel Co.*, 193 F. 2d 461 (2d Cir. 1952), cert. denied, 343 U.S. 956 (1952), decided over a decade ago, the Court of Appeals for the Second Circuit held that the rights created by Rule 10(b)-5 "extended only to [a] defrauded purchaser or seller." All the arguments advanced by plaintiff here were expressly rejected by that Court in its opinion by Judge Augustus N. Hand, in which Judge Learned Hand and Chief Judge Swan joined. Indeed, the opinion reads as if it were written for the specific purpose of considering and disposing of plaintiff's contentions in this case and is therefore set out at length (p. 463-64):

> The appellants contend that the applicability of the rule is not limited to the actual purchasers or sellers of securities, but that the general proscription of fraud "upon any person" includes and supplements the common law liability of those who abuse the trust of their corporate positions. They contend that this construction is further supported by the use of the words "in connection with" the purchase or sale of securities; for, if the intent had been to deal with just the purchase or sale of securities, the words "in connection with" are superfluous and would not have been added.
>
> While the Rule may have been somewhat loosely drawn its meaning and scope are not difficult to ascertain when reference is had to the scheme of SEC Regulation and the purpose underlying the adoption of X-10B-5. Prior to its adoption the only prohibitions against fraud in the sale or purchase of securities were contained in Section 17(a) of the 1933 Act, 15 U.S.C.A. § 77q(a), and § 15(c) of the 1934 Act, 15 U.S.C.A. § 78o(c). Section 17(a) of the 1933 Act only made it unlawful to defraud or deceive *purchasers* of securities, and Section 15(c) of the 1934 Act dealt only with

fraudulent practices by security brokers or dealers in over-the-counter markets. No prohibition existed against fraud on a seller of securities by the purchaser if the latter was not a broker or a dealer. Consequently, on May 21, 1942 the SEC adopted Rule X-10B-5 to close this "* * * loophole in the protections against fraud administered by the Commission by prohibiting individuals or companies from buying securities if they engage in fraud in their purchase." SEC Release No. 3230, May 21, 1942. See Note, 59 Harv. L. Rev. 769, 770; Fischman v. Raytheon Mfg. Co., 2 Cir., 188 F. 2d 783, 787, n. 2. The SEC's press release, above quoted, which announced the Commission's adoption of Rule X-10B-5, shows that the Commission was attempting only to make the same prohibitions contained in Section 17(a) of the 1933 Act applicable to purchasers as well as to sellers. That such was the only purpose of Rule X-10B-5 is made abundantly clear when the language of the Rule is compared with the language of Section 17(a); the Commission simply copied Section 17(a), adding the words "any person" in place of "the purchaser" and a final clause "in connection with the purchase or sale of any security."

But the appellants argue that such an interpretation of the Rule is too narrow to carry out the broad purpose of the Act to protect investors "from exploitation by corporate insiders." See Hearings before Senate Comm. on Banking and Currency on S. Res. 84, 56 and 97, 73d Cong., 1st Sess., pp. 6456-6. We do not doubt that Congress was at least partially motivated by such a purpose in enacting the Securities Exchange Act of 1934, 15 U.S.C.A. § 78a et seq. However, the precise question here is whether Section 10(b) of that Act and the Commission's Rule X-10B-5 were the means chosen to further that end, and we are of the opinion that the legislative "history" and "purpose" quoted by appellants are not persuasive that they were. When Congress intended to protect the stockholders of a corporation against a breach of fiduciary duty by corporate insiders, it left no doubt as to its meaning. Thus Section 16(b) of the Act of 1934, 15 U.S.C.A. § 78p(b), expressly gave the corporate issuer or its stockholders a right of action against corporate insiders using their position to profit in the

sale or exchange of corporate securities. The absence of a similar provision in Section 10(b) strengthens the conclusion that that section was directed solely at that type of misrepresentation or fraudulent practice usually associated with the sale or purchase of securities rather than at fraudulent mismanagement of corporate affairs, and that Rule X-10B-5 extended protection only to the defrauded purchaser or seller.

In the years since *Birnbaum*, its ruling has been consistently adhered to.[3] The suggestion of plaintiff that the Second Circuit has withdrawn or modified its ruling in *Birnbaum* is patently contradicted by its most recent approval of the decision in *O'Neill* v. *Maytag*, 339 F. 2d 764 (2d Cir. 1964).

Not only is the construction given by the Seventh Circuit in the instant case supported by the case law and by administrative action (since no attempt has been made by the SEC to amend Rule 10(b)-5), but, in addition, Congress has repeatedly rejected attempts to amend the law to expand the coverage of Section 10(b) beyond sellers and buyers.

Thus, in 1956, bills were introduced in Congress to amend Sec. 10(b) of the Securities Exchange Act of 1934 by adding the phrase "or proposed purchase or sale." S. 3915, H.R. 11,129, 84th Congress, 2nd Session (1956). These bills were not enacted.

In 1957 and again in 1959, similar bills were introduced in Congress to amend Sec. 10(b) of the Securities Exchange Act of 1934 by adding the phrase "or any attempt to pur-

---

[3] *Joseph* v. *Farnsworth Radio & Television Corp.*, 198 F. 2d 883 (2nd Cir. 1952); *Brouk* v. *Managed Funds, Inc.*, 286 F. 2d 901 (8th Cir. 1961), cause remanded on suggestion of mootness, 369 U.S. 424 (1962); *Hooper* v. *Mountain States Securities Corporation*, 282 F. 2d 195 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961); *Keers & Company* v. *American Steel and Pump Corp.*, 234 F. Supp. 201 (S.D.N.Y. 1964); *Kremer* v. *Selheimer*, 215 F. Supp. 549 (E.D. Penn. 1963); and *Donovan, Inc.* v. *Taylor*, 136 F. Supp. 552 (N.D. Calif. 1955).

chase or sell." S. 2545, H.R. 9327, 85th Congress, 1st Session (1957); S. 1179, H.R. 2480, 86th Congress, 1st Session (1959). Again, these proposed changes were rejected by Congress.[4]

It is clear, therefore, that the limitation of the Rule to purchasers and sellers has been consistently adhered to by the courts and Congress. These authorities demonstrate that plaintiff's arguments are neither novel nor meritorious.

The conflict "in principle" which plaintiff purports to find between the decision of the Court of Appeals below and the decisions of other courts does not exist. None of the cases cited by plaintiff are inconsistent with the ruling in *Birnbaum*. None of the cases extends Rule 10(b)-5 to give standing to sue to anyone other than "a defrauded purchaser or seller" of securities.

2. The case is moot

Plaintiff asks this Court to review a judgment of the Court of Appeals dissolving a preliminary injunction which had restrained Schenley from forwarding checks in payment of accepted shares tendered and purchased in response to the Invitation for Tenders and from returning certificates for shares tendered but not purchased.

Plaintiff did not tender his shares. Plaintiff does not and could not seek a rescission of any transaction with defendant Schenley nor any other non-injunctive relief. Insofar as plaintiff suggests a remedy of rescission, he is asserting a claim on behalf of a class of which he is not a member since he did not tender his shares under the Invita-

---

[4] See 103 Cong. Record 11636; SEC Legislation, Hearings before a Subcommittee of the Committee on Banking and Currency of the U.S. Senate, 86th Congress, 1st Session (1959) 331. 3 Loss, Securities Regulation (2d ed. 1961), 1424, fn. 6.

tion and his interests as a non-selling shareholder may conflict with those of selling shareholders.[5]

As the plaintiff himself points out in his Petition for Certiorari (p. 9 and p. 24) the transaction has been fully completed. The relief sought by plaintiff has become moot.

If this plaintiff as a stockholder can establish a case of waste or mismanagement in the corporation's purchase of its shares, he may pursue his remedy under Count II. What this plaintiff—neither a purchaser nor a seller—may not do, under the established *Birnbaum* doctrine as properly applied by the court below, is to use Rule 10(b)-5 as a vehicle to enforce a State-law claim of waste or mismanagement that happens to involve a purchase of securities from others.

Plaintiff is here seeking a review of an academic question. It is not this Court's function to give such an advisory opinion. This Court has long held that it will not render decisions on academic or moot questions of law. *Richardson* v. *McChesney*, 218 U.S. 487, 492 (1910); *Brownlow* v. *Schwartz*, 261 U.S. 216, 217 (1923).

CONCLUSION

For the foregoing reasons it is respectfully submitted that the Petition for Certiorari herein should be denied.

Respectfully submitted,

SIDNEY R. ZATZ
HOWARD ARVEY
MILTON H. COHEN
Attorneys for Respondent

Of Counsel:

PEYTON FORD

---

[5] The undetermined complaint in the *SEC* v. *Texas Gulf Sulphur Company* case, CCH Fed. Sec. L. Rep. ¶ 91,520 (1965), has no conceivable factual or legal connection with this case.

LIBRARY
SUPREME COURT, U.S.

No. 182

~~No. 1209~~

Office-Supreme Court, U.S.
FILED
AUG 4 1965
JOHN F. DAVIS, CLERK

In the

Supreme Court of the United States

OCTOBER TERM, 1964

STANLEY JACHIMIEC, individually and on behalf of all other similarly situated shareholders of SCHENLEY INDUSTRIES, INC.,

Petitioner,

vs.

SCHENLEY INDUSTRIES, INC., a corporation, W. E. BLAKELEY, E. R. DEUTSCHE, THEODORE GOMMI, MILO B. HOPKINS, P. E. LOCKWOOD, JOHN MACKIE, E. S. MONOHAN, J. LINCOLN MORRIS, MILTON J. NAUHEIM, L. B. NICHOLS, LEWIS S. ROSENSTIEL, A. D. SCHULTE, R. G. SMITH and THEODORE C. WIEHE,

Respondents.

REPLY BRIEF OF PETITIONER IN SUPPORT OF PETITION FOR CERTIORARI

MILTON V. FREEMAN
1229 Nineteenth Street, N.W.
Washington, D.C.

HOWARD R. KOVEN
SHELDON O. COLLEN
208 South LaSalle Street
Chicago, Illinois
Attorneys for Petitioner

Of Counsel:
ARNOLD, FORTAS & PORTER
1229 Nineteenth Street, N.W.
Washington, D.C.

The Scheffer Press, Inc.—ANdover 3-6850

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1964

No. 1209

STANLEY JACHIMIEC, individually and on behalf of all other similarly situated shareholders of SCHENLEY INDUSTRIES, INC.,

Petitioner,

vs.

SCHENLEY INDUSTRIES, INC., a corporation, W. E. BLAKELEY, E. R. DEUTSCHE, THEODORE GOMMI, MILO B. HOPKINS, P. E. LOCKWOOD, JOHN MACKIE, E. S. MONOHAN, J. LINCOLN MORRIS, MILTON J. NAUHEIM, L. B. NICHOLS, LEWIS S. ROSENSTIEL, A. D. SCHULTE, R. G. SMITH and THEODORE C. WIEHE,

Respondents.

REPLY BRIEF OF PETITIONER IN SUPPORT OF PETITION FOR CERTIORARI.

---

1. Respondent's Brief in Opposition does not in any way contest the importance of the questions presented as set forth in the Petition. Its only argument is the contention that the legal principle in the case below (as construed by it) is correct and consistent with previous rulings rather than, as we have argued, that the principle is incorrect and in conflict with previous rulings of this Court and other courts.

2. In respect to the conflict with other rulings we rely on the presentation set forth in our Petition. We assert

that even if it were true (which it is not) that the lower courts in other circuits would be unanimous in adopting the narrower ruling of the court below, the issue presented by this case is, for the reasons stated, of the greatest importance and a pronouncement by this court is required. In addition, as stated on pages 22 to 24 of the Petition, it is clear that the present case is inconsistent with the rulings of this Court and of the Third and Fifth Circuits and that the *Birnbaum case* (193 F. 2d 436), quoted by Respondent at such great length, whatever its authority*, does not apply to the broad denial in this case of plaintiff's standing to sue.

3. This case is in no sense moot. The issue is solely standing to sue for it is clear that if plaintiff has standing to complain of the false solicitation material, the court can and may shape remedies, *e.g.* rescission on the basis of further disclosure, and other remedies set forth in the last paragraph of the Petition (p. 25), as well as additional remedies which may appear appropriate after trial. *J. I. Case Co.* v. *Borak*, 377 U.S. 426. Of course, if Petitioner has no standing, as Respondent contends, then he has no right to complain, but this is not because the case is moot but because the issue in controversy would be a matter of no concern to him.

4. However it is just this issue of standing to sue which is consequential. The issue whether a shareholder-

---

* The *Birnbaum* court characterized the situation (193 F. 2d 436, 464) as essentially fraudulent mismanagement of corporate affairs, in contrast to "fraudulent practices usually associated with the sale or purchase of securities."

It does not follow, of course, that even the *Birnbaum* court would have disqualified a shareholder-offeree from suing, since the fact remains that "an offer to purchase" (not involved in *Birnbaum*) is patently an act or transaction "in connection with the purchase or sale of securities."

offeree has a right to complain of a false tender invitation is clearly of great importance; the limitation of standing to sue which the lower court imposed, confining the remedy only to those offerees who blindly accepted the offer, raises the vital questions of public policy which are set forth in detail in the Petition (pp. 14-22).

5. The argument that the tender invitation was not false and misleading underscores the existence of issues to be tried. Respondent argues (Br. p. 4) that the earnings we have called "extraordinarily improved" are arrived at by "the device of not using the same factors" for the periods being compared. The footnote (Br. p. 4) refers to a "nonrecurring" capital gain which "obviously" must be disregarded. It refers also to the interest in the earnings of Buckingham Corporation acquired on August 31. We will not burden the court with rebuttal on the merits. We point out only that these arguments plainly cannot be disposed of on the Complaint alone or by assertions of counsel in opposition to the Petition for Certiorari. They require presentation of testimony and the exploration of the facts as to *e.g.*:

a. When the "nonrecurring" capital gain occurred;

b. What its significance is;

c. What the Buckingham Corporation is;

d. What the reasons are for inclusion or non-inclusion of its earnings; and

e. When, with respect to the time of the tender offer and the delivery of the securities, the "extraordinarily improved" earnings became known to the management.

These considerations are, of course, in addition to the other important factual considerations concerning, *e.g.* the "approaches" to the major stockholders to sell their shares and the extent to which the approaches were "definitive" as to price (Ptn. pp. 8-11). Patently, the facts must be determined on trial by testimony and other evidence and not by argument from the face of the document.

CONCLUSION.

The Petition for Certiorari in this case presents important questions concerning the application of the federal securities laws and should be granted.

Respectfully submitted,

MILTON V. FREEMAN
1229 Nineteenth Street, N.W.
Washington, D.C.
HOWARD R. KOVEN
SHELDON O. COLLEN
208 South LaSalle Street
Chicago, Illinois
Attorneys for Petitioner

Of Counsel:
ARNOLD, FORTAS & PORTER
1229 Nineteenth Street, N.W.
Washington, D.C.